



GLOBAL INSIGHT

The World Economy Faces Headwinds from a U.S. Recession

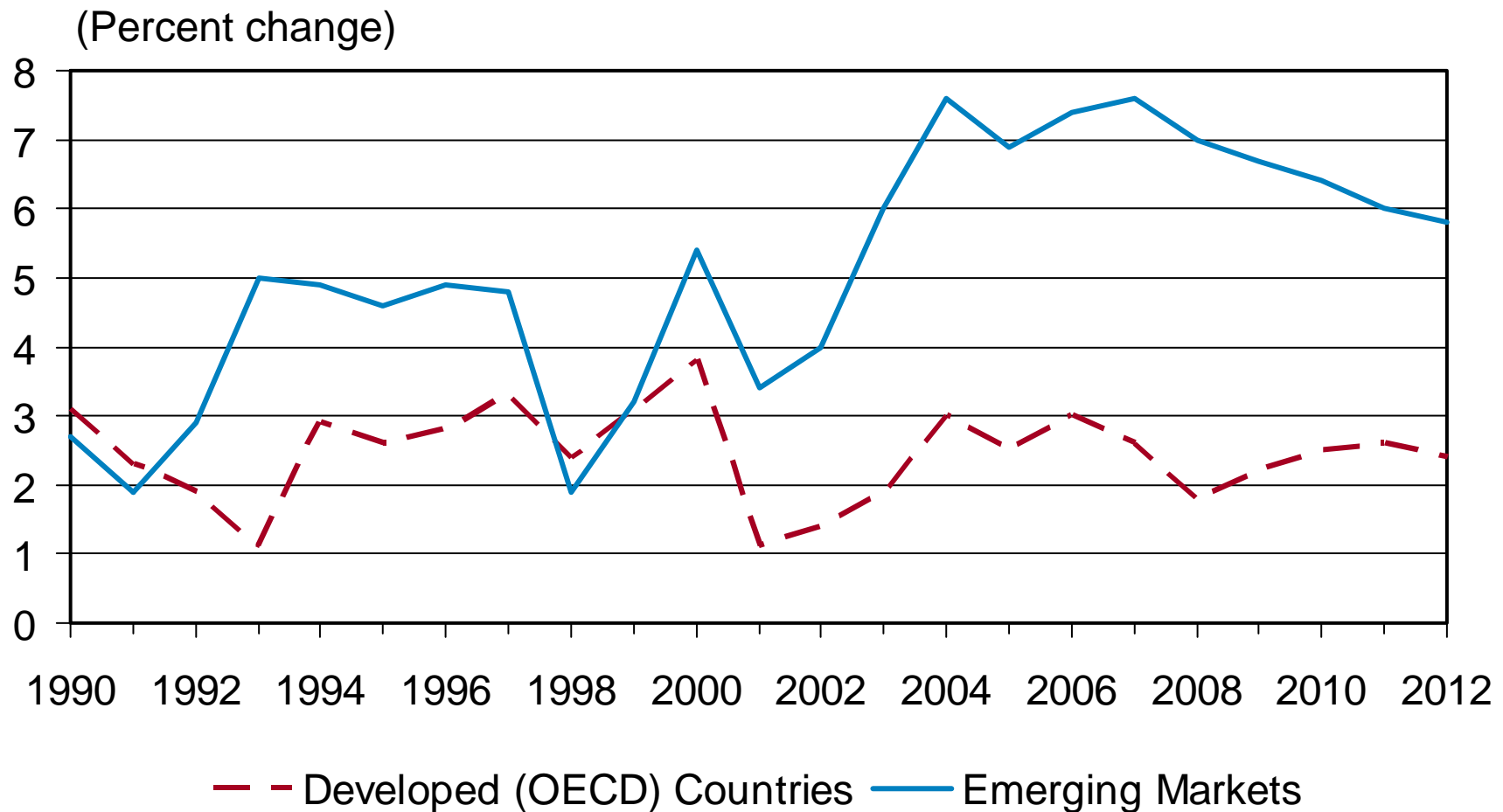
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FAA
March 10, 2008

The Global Outlook: Slower Growth Ahead

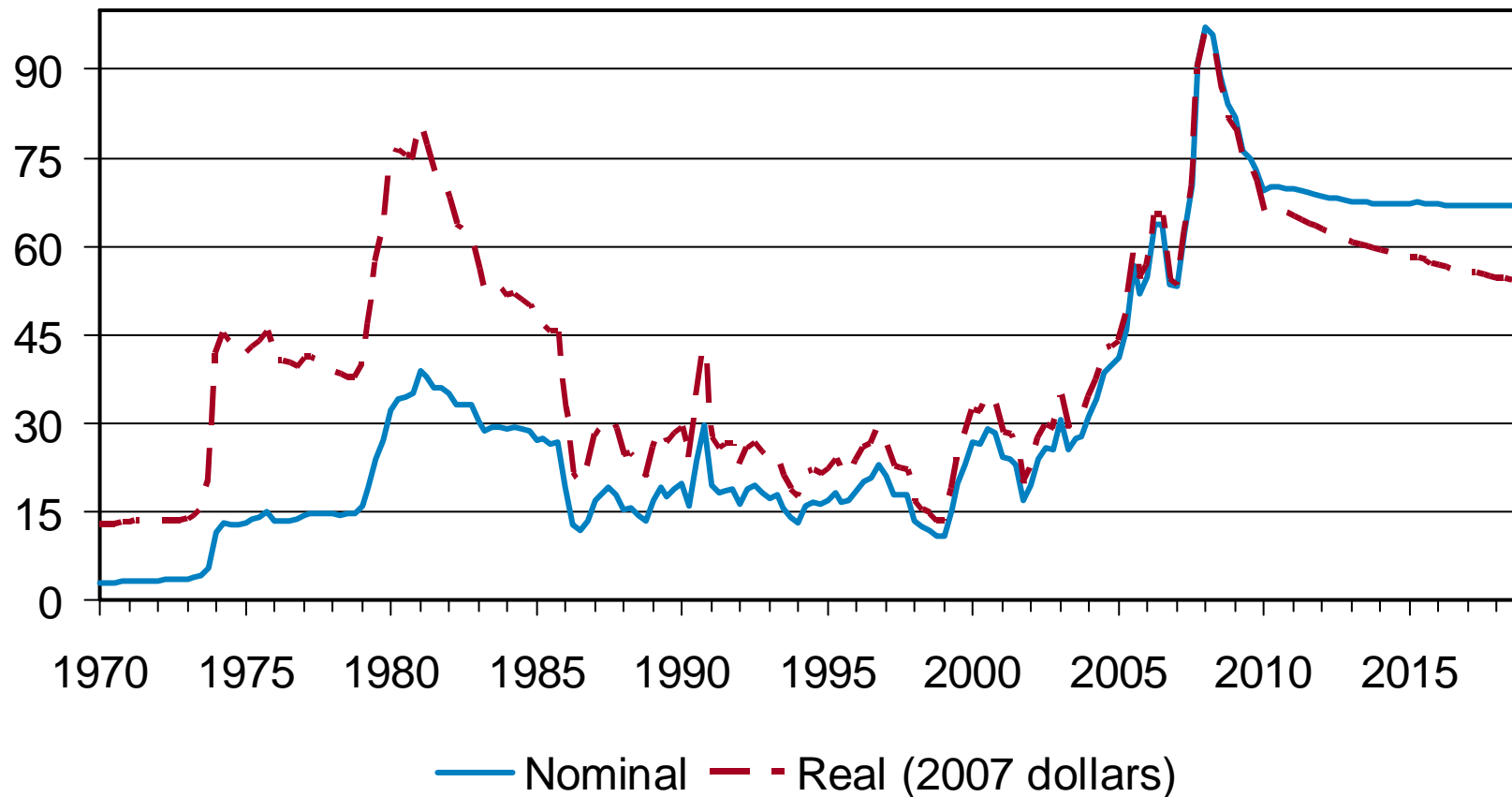
- **A global economic slowdown is under way, exacerbated by financial market turbulence**
- **The U.S. economy has slipped into a mild recession**
- **Europe faces headwinds from rising currencies, tightening credit, and house price corrections**
- **With its export engine slowing, China's investment boom could turn into a post-Olympics bust**
- **Emerging markets are better positioned than in 1997-98, but vulnerable to a China hard landing**

A Two-Speed World: Real GDP Growth

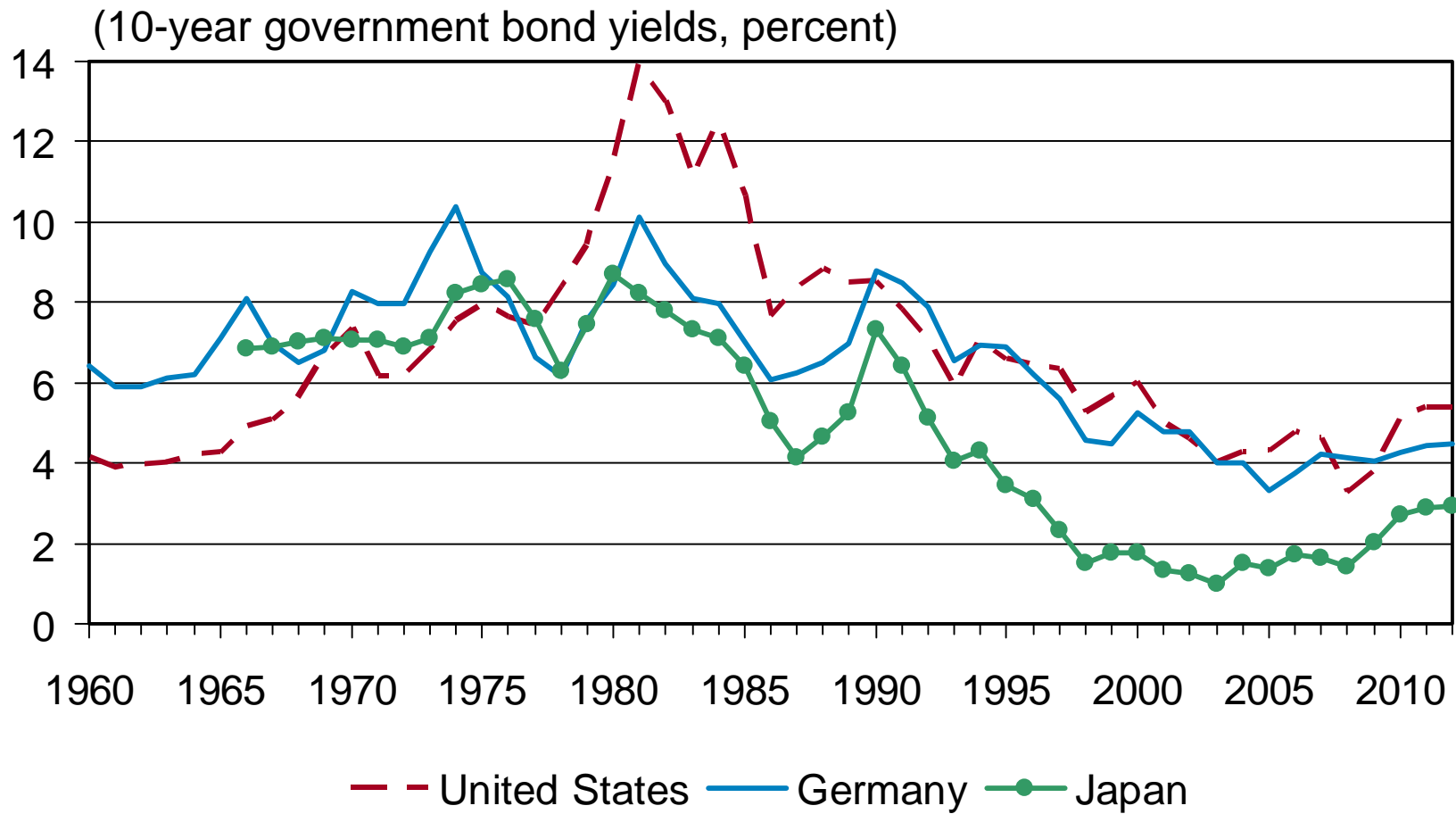


Real Crude Oil Prices Will Eventually Come Down

(U.S. refiners' acquisition price of imports, \$/barrel)



Long-Term Interest Rates Are Relatively Low

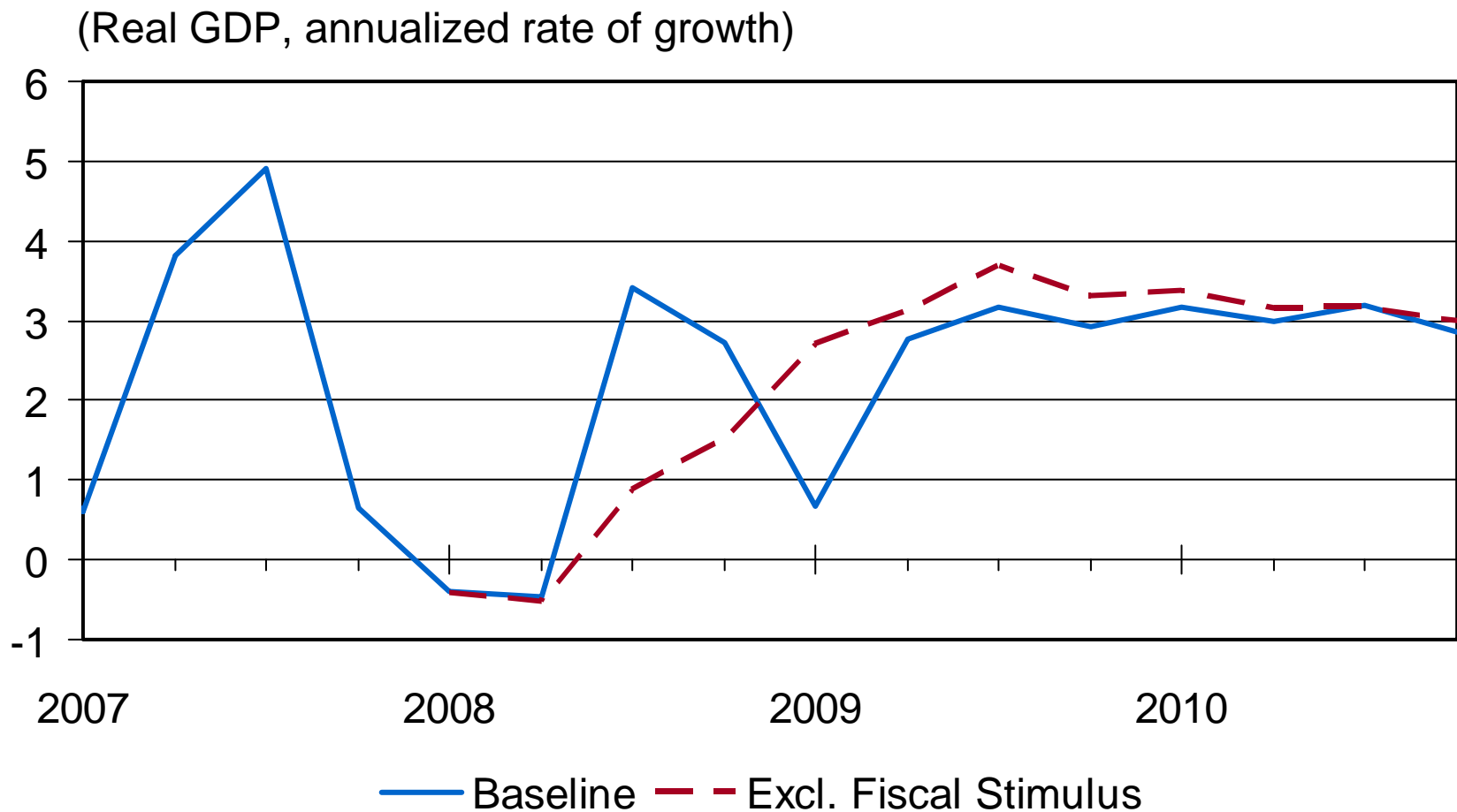


The U.S. Economy in the Danger Zone

- The housing crash, credit crunch, and high oil prices have stalled U.S. economic growth
- Home sales, prices, and construction will fall further
- Consumers will spend more cautiously
- Capital spending and job growth will slow
- A bright outlook for exports, combined with low inflation/interest rates and fiscal stimulus will limit the depth and duration of the recession

Plan for a mild U.S. recession

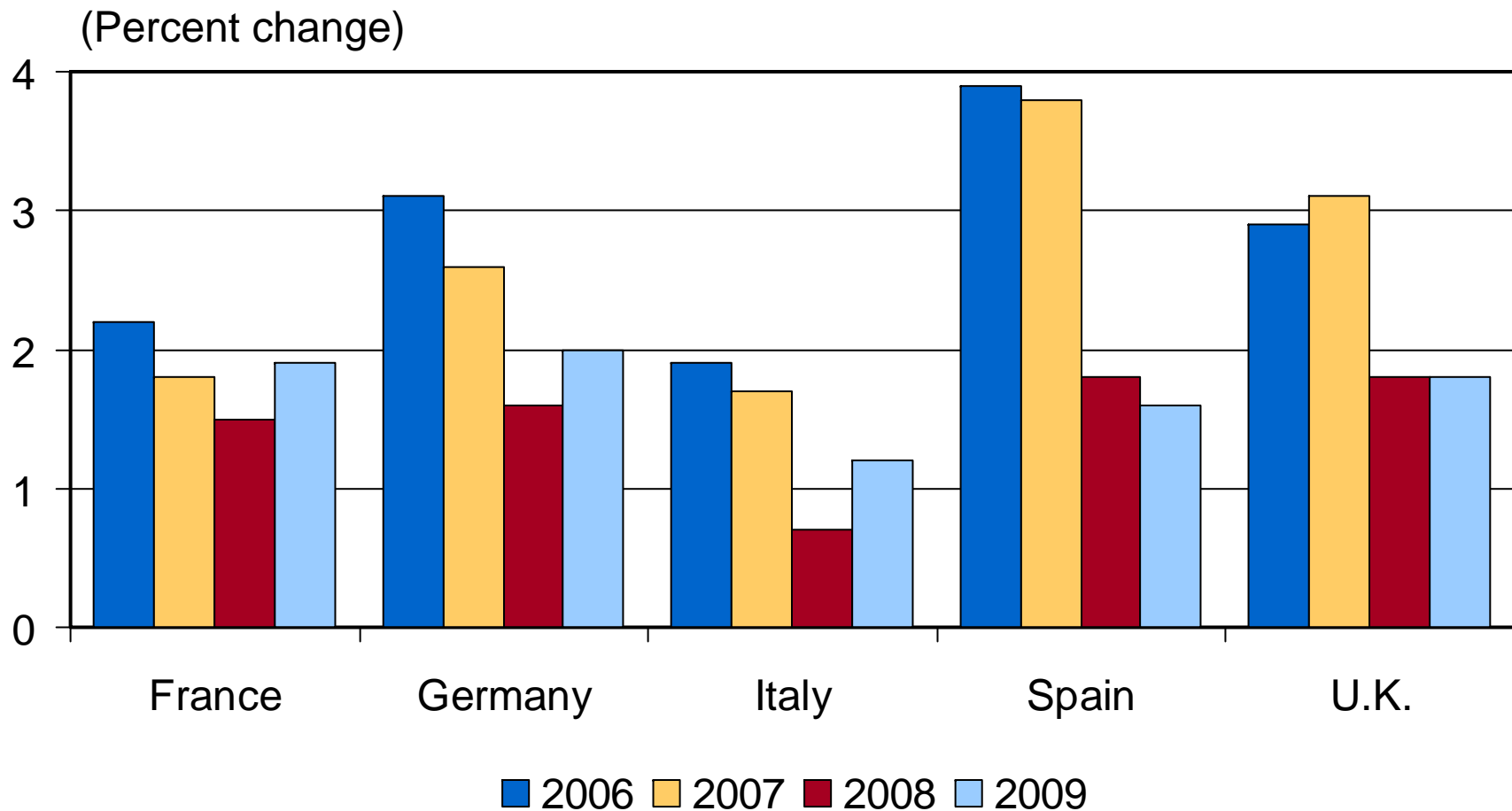
Fiscal Stimulus Pulls Growth Into 2008 – GDP



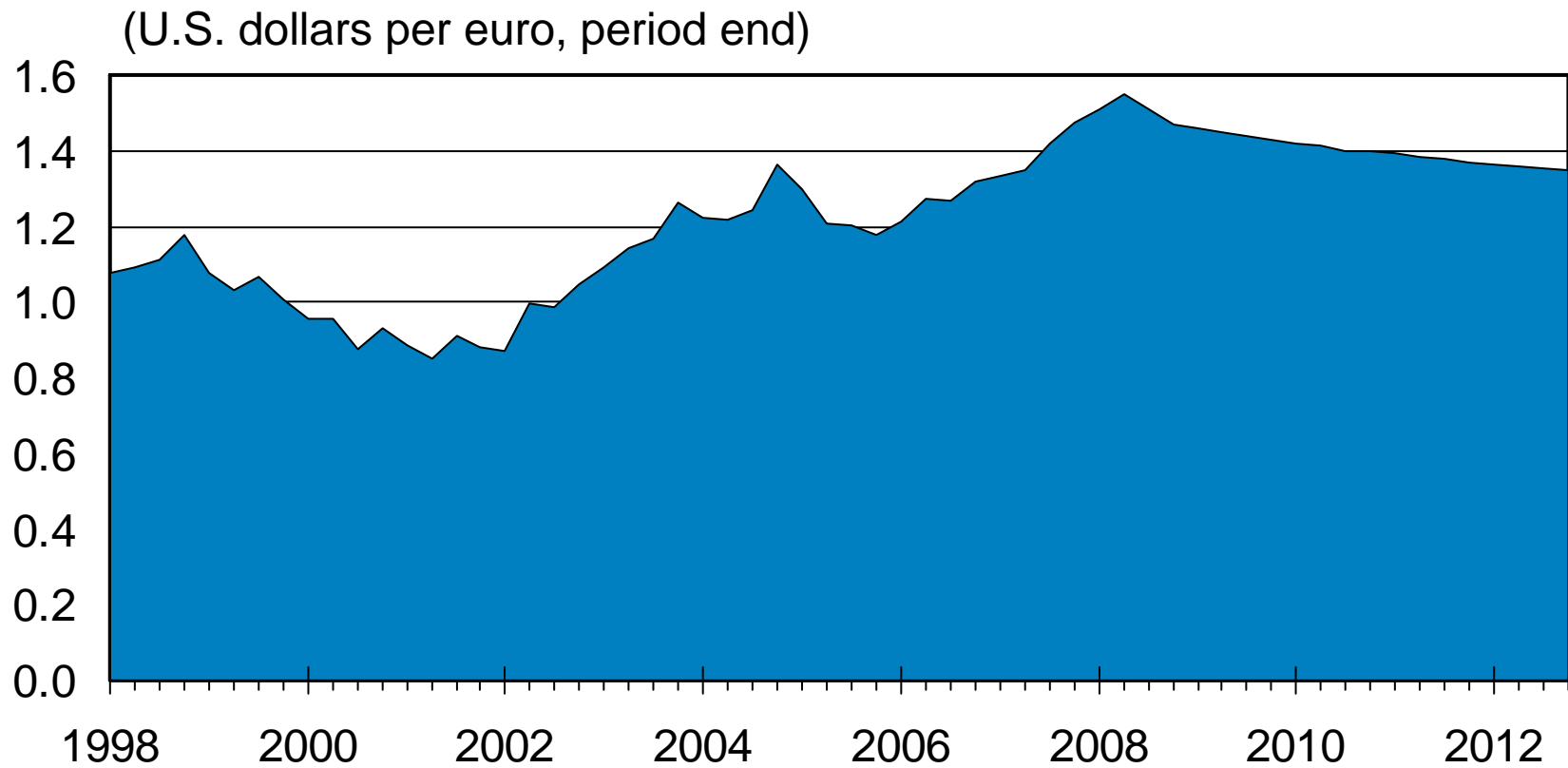
Western Europe Economies Losing Momentum

- **Financial institutions have significant exposure to the U.S. subprime mortgage problems**
- **The credit crunch and appreciating currencies will slow capital spending and exports**
- **Housing market corrections pose risks in Spain, Ireland, the United Kingdom, and France**
- **Limits on long-term growth – demographics, policy**
- **North/South competitiveness divide in unit labor costs**

Real GDP Growth Rates Vary Across Europe



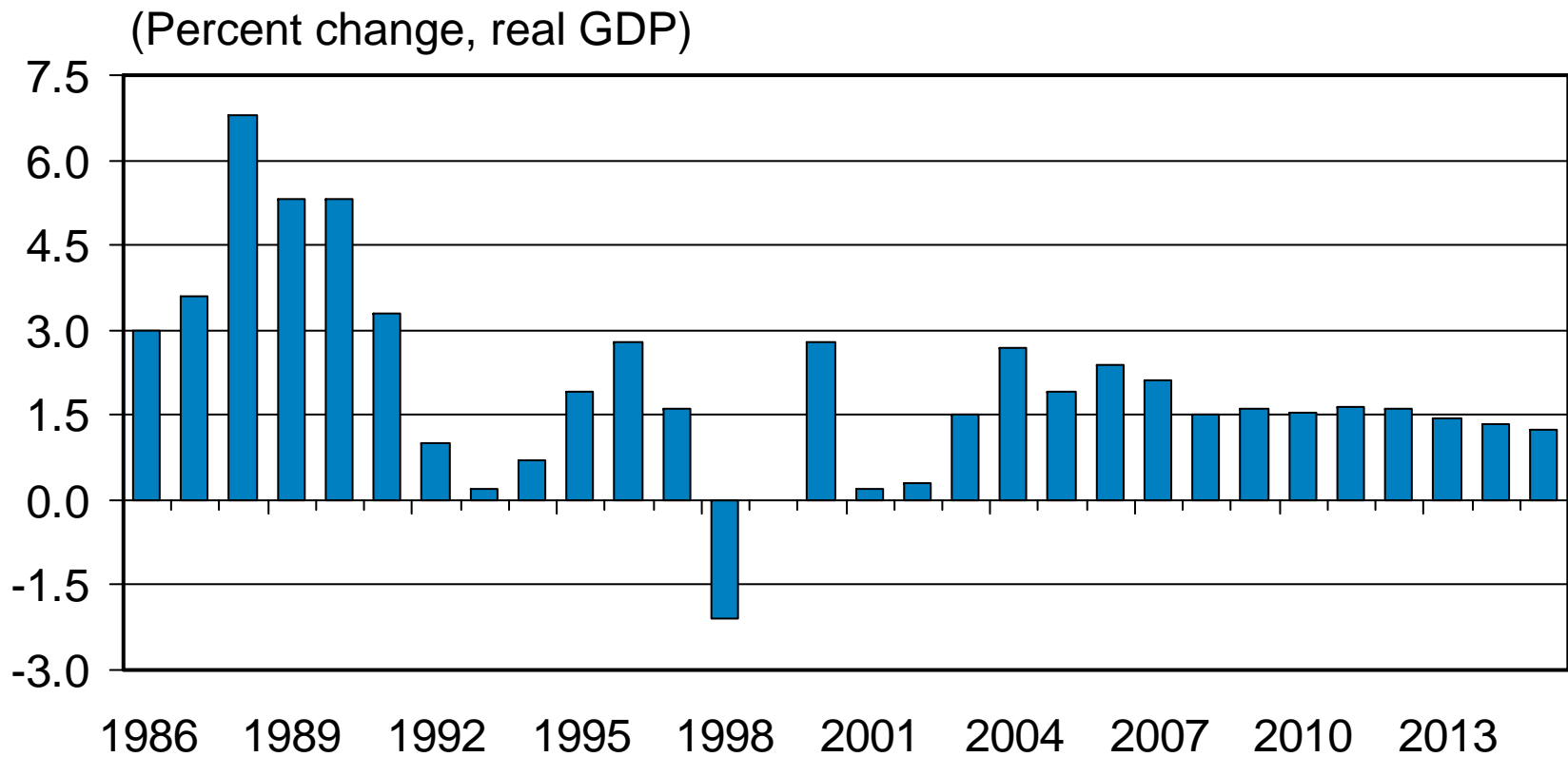
The Euro Will Appreciate Through Mid-2008



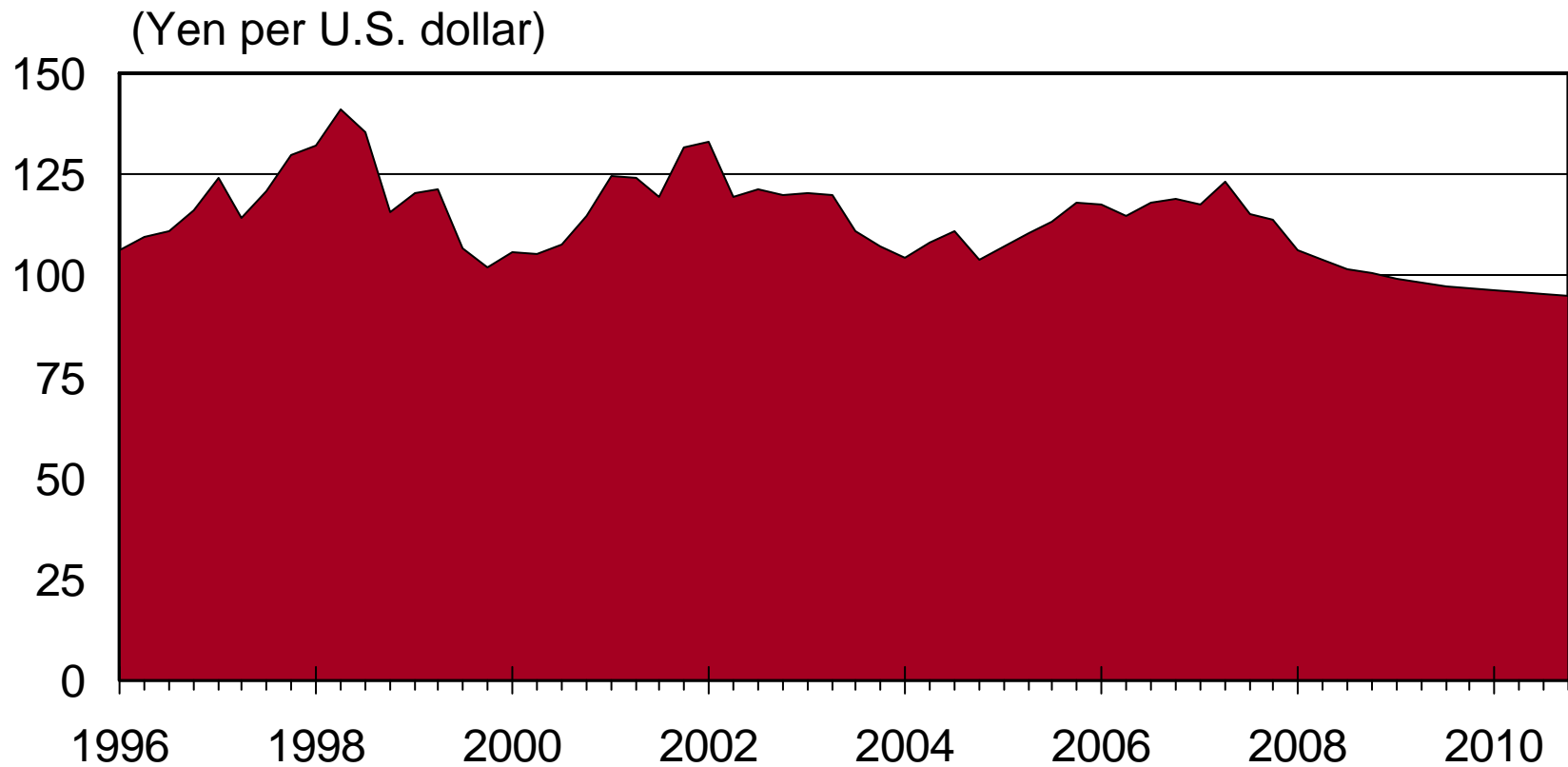
Japan Settles on a Slow Growth Path

- **The engine of growth will (hopefully) shift from exports to consumer spending**
- **The yen's appreciation will continue**
- **Political divisions will slow economic reforms**
- **Inflation and interest rates will gradually rise**
- **Japan's population has entered a long-term decline**
- **Trend growth will slow from 2% to 1% in next 10 years**

Japan's Economy Has Limited Growth Potential



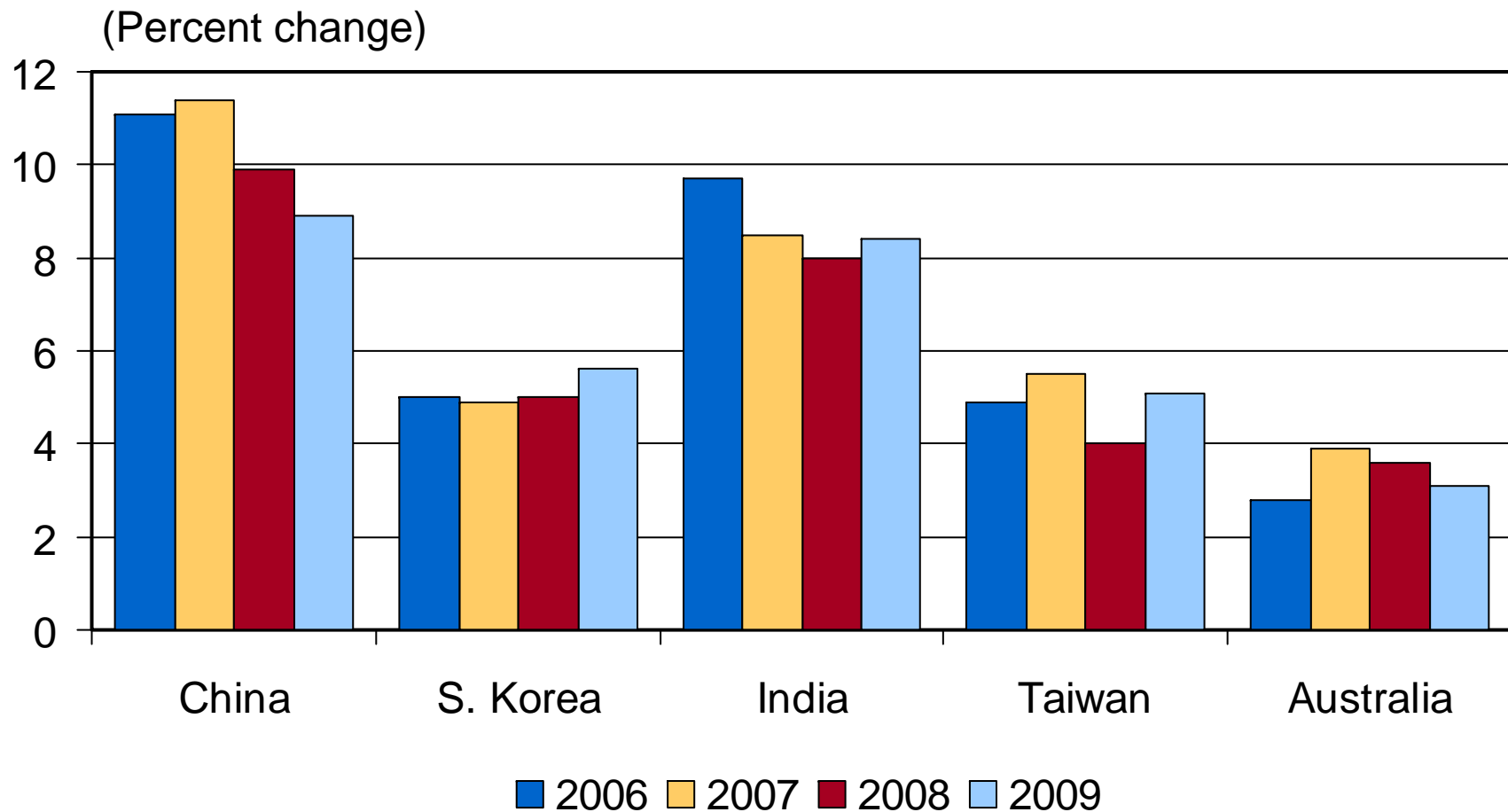
The Dollar Will Depreciate Against the Yen



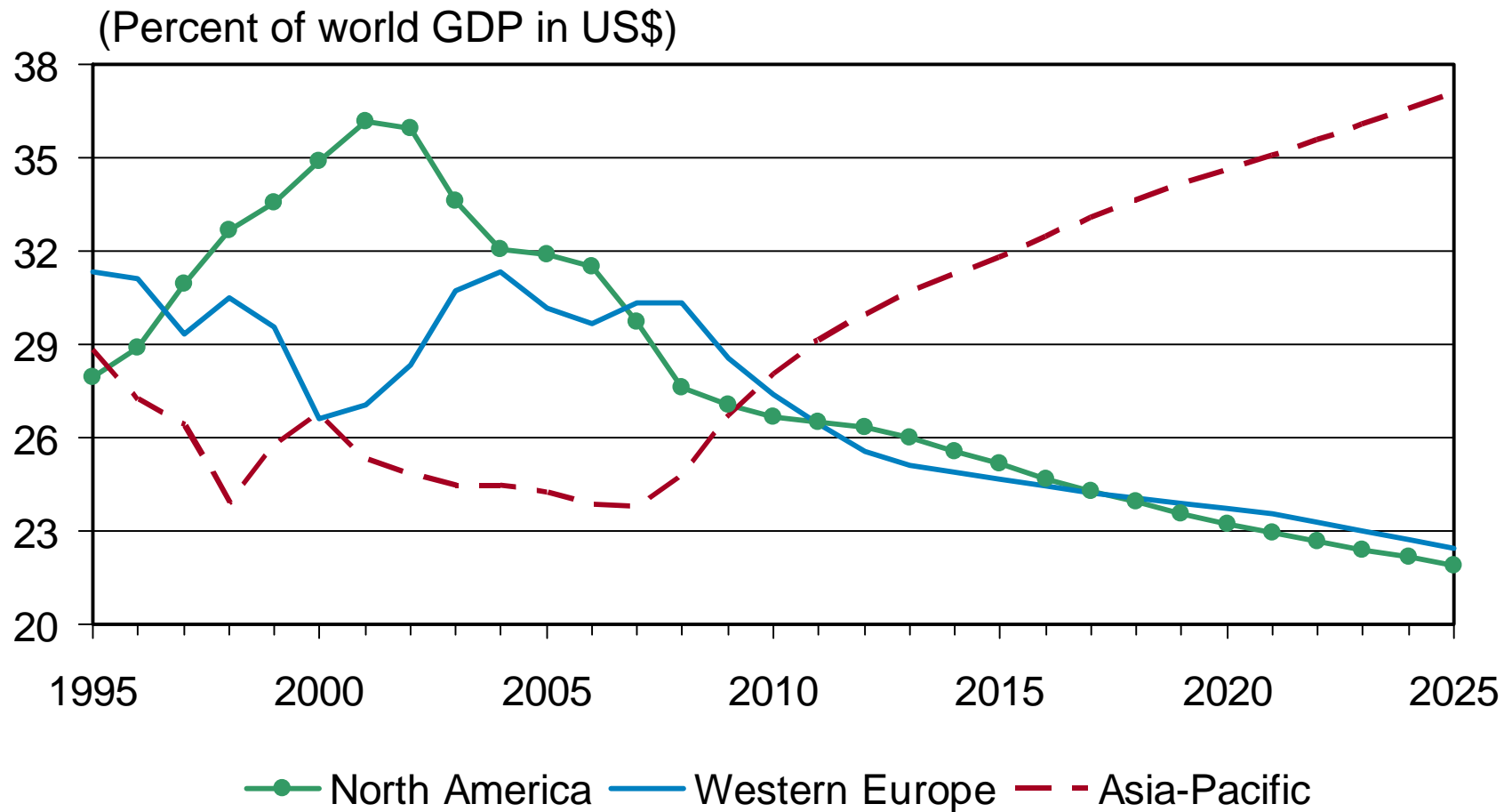
Emerging Asia Is Powering Global Growth

- **Momentum will shift gradually from exports to domestic demand**
- **China's overheated investment boom continues; the risk of a post-Olympics hard landing is rising to between 35% and 40%**
- **India is relatively immune from global financial turmoil**
- **High saving rates → Asia remains an exporter of capital**
- **Exchange rates across Asia will rise**

Real GDP Growth in Asia-Pacific Economies



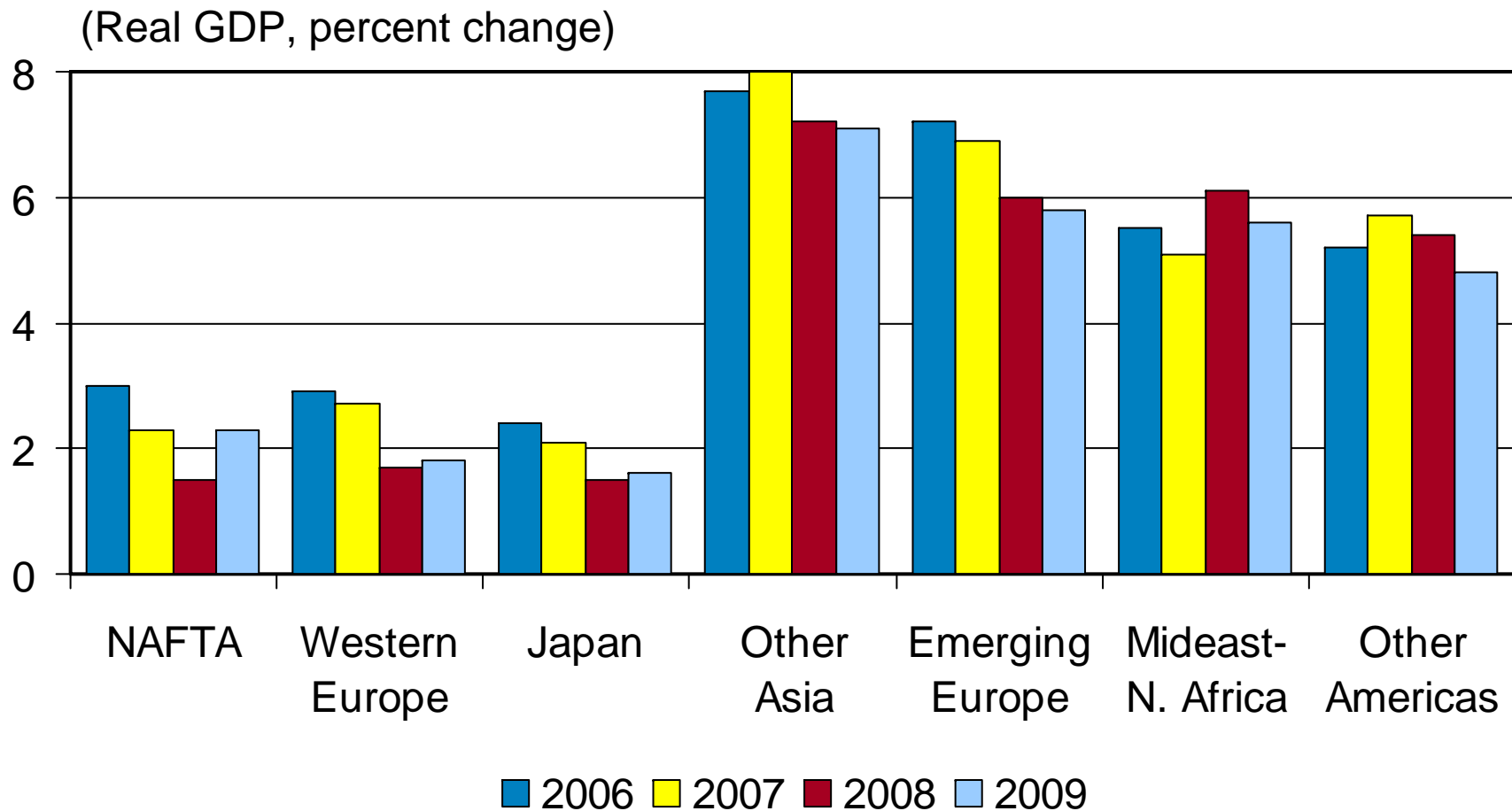
Asia's Rising Share of World GDP



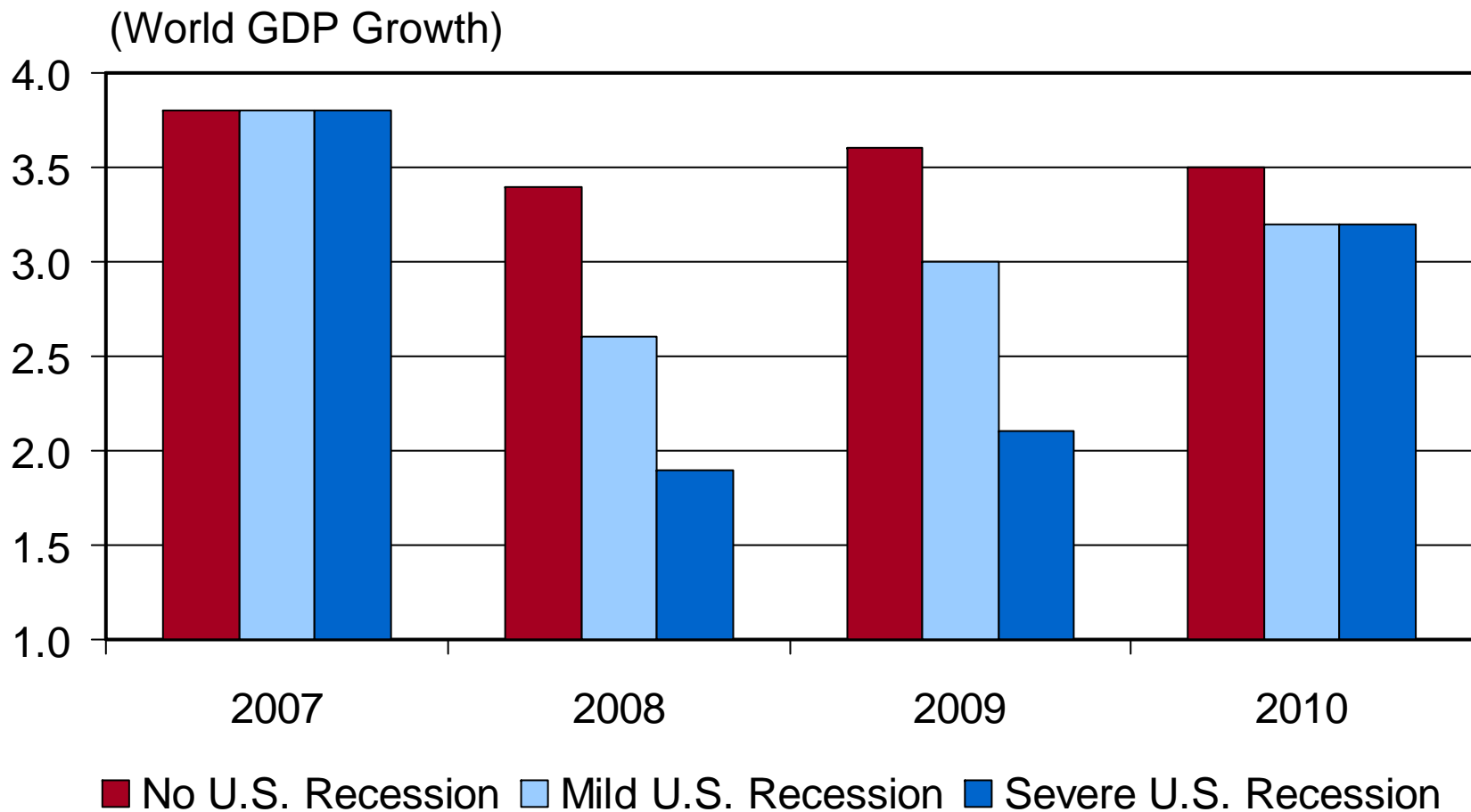
Emerging Markets Boom Might Be Ending

- **Achieving best sustained growth in decades**
- **Stronger financially – trade and fiscal balances, foreign exchange reserves**
- **Flight from risk could restrain investment inflows**
- **Sharp deceleration in U.S. imports will hurt**
- **Commodity exporters vulnerable to price correction, especially if Chinese growth falters**
- **Boom times have reduced the urgency of reforms and encouraged “resource nationalism”**

Wide Variations in Regional Economic Growth



The Risks to Global Growth from a U.S. Recession



Bottom Line

- **Global expansion continues at a slower pace**
- **The credit crunch poses significant downside risks**
- **The U.S. economy has slipped into a mild recession**
- **Japan and the Eurozone have limited growth potential**
- **China's boom could lead to a post-Olympic bust**
- **Emerging markets will do well, as long as China's growth holds up**
- **The probability of a world recession remains low – no more than 25%**